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## LIQUIDATION TAXES

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It is indicative of the advance of economic thought that in the present war its main controversy should turn on the relative merits of taxes and loans. There are few economic principles but which are put in a fresh light by the discussion which bids fair to make as important changes in economic theory as did the famous rent controversy during the Napoleonic wars. This older discussion emphasized the presence or absence of an unearned element in income. Land incomes were put in a separate class with a resulting pressure to relieve industry from taxation by putting the burden on land revenues. The sweep of free trade doctrines could hardly have been as complete as it was if the rent controversy had not preceded it. We may expect a like transformation of economic doctrine if the relative merits of taxes and bond issues are settled as permanently as were the issues involved in the discussion of rent and free trade. Every great fallacy in thought discovered and removed makes possible new adjustments not only to nature but also between the various social groups on whom industrial efficiency depends.

The evils of taxation, however, do not make bond issues good nor those of bonds make taxes the only way to meet national burdens. Earlier controversies revealed that protection was bad without proving that free trade was good; that paper money made a disastrous form of inflation without showing that other expedients did not have like evils; that rent was an unearned income without giving an economic justification to kindred forms of income. In each case the advance consisted in barring out one expedient without increasing the respect for the others. I anticipate a like result in this case. I doubt if the opposition to taxation will be reduced by the controversy but I believe that in the end bond issues as an expedient to carry on a great war will have no better standing than paper money now has. We must learn to get on without bonding just as we have learned how to promote industry without protection or to meet urgent obligations without a resort to paper money. Nor

do I wish this paper to be viewed as an eulogy of taxation; but I desire to show that large bond issues are a fatal expedient, something that we cannot use without the danger of social disintegration. Beyond this I wish to show that its reputed advantages are illusory, destroying and not conserving our resources. It would be useless to show this if it were not accompanied with positive information as to how to devise an adequate tax system. If we do not want the public to use patent medicine we must provide sane remedies. In the same way the opponent of bond issues must show how extraordinary expenses can be met without their use. The present task is to devise a system that will meet the need for revenue and yet avoid bond issues to the same degree that a sound financial system avoids paper money

#### OBJECTIVE TESTS

Economics is now becoming like physical science in that only objective tests are used. So long as economists asked how do men feel about certain measures no reply could be made but to test these feelings, or to appeal to certain supposed innate principles at the basis of human psychology. There was no way to determine these feelings except in small communities composed of like individuals. The method used was to assume a typical man and to get at the assumed advantage or disadvantage by multiplying the sum of his feelings by the number of the people concerned. Such a method fails in a great nation with many classes and many grades of income each resulting in certain feelings peculiar to his class. This complex cannot be summed into a whole because the advantage of one group may arise from the disadvantage of another. We thus have society split up into a number of classes each with its own measures and each assuming the falsity of other standards than those it uses. From this confusion there is no exit except by discarding all subjective measurements and by proceeding according to objective tests such as physical science employs. Great advance has been made in recent years in collecting the data by which objective tests can be applied. We are now in a position where objective tests will produce better results than subjective methods. What we feel and what we know in many fields clash. Only as we suppress the feeling and permit the facts to guide can we hope to attain the objective adjustment on which the permanent prosperity depends. We may

blunder along in times of peace because the cost of bad action is not severe enough to strangle the life of a nation, but the drain of a war is too great to permit of the waste which our feelings in times of peace encourage. In war the nations or group of nations will win which succeeds in preventing waste. We may outrage our feelings without serious loss if we conserve our resources. The older subjective economics thus fails to solve our problems. It is the newer objective science to which we must resort.

### THE PHYSICAL COST OF WAR

The first problem to face in this objective way is the physical cost of the war. We are so used to figure in terms of values that we seldom think just what these values stand for. Values are estimates based on income and grow or decline as income is altered. If the return from property is estimated at 4 per cent instead of 5 per cent we immediately assume we are to have a quarter more wealth. If a property yields \$5,000 instead of \$4,000 we immediately assert that we are correspondingly more wealthy. Our estimates which make us as a nation worth two hundred billion dollars are of this nature. No one has made an actual investigation to find what property we have. We estimate its amount from the revenue it yields. But mere values cannot carry on a war. War destroys physical goods and their amount fixes the contribution which each nation may make. The cost of the war is the destruction of these goods, losses for which fresh labor is needed to replace. We may through inflation think we are getting rich because values rise and yet we may be losing the basis on which our prosperity depends. On the other hand we may lose much that hurts our feelings, and yet be as capable as ever of prosecuting the war. We often lament the loss of non-essentials more severely than that of the more substantial elements of personal welfare. Our estimates must conform to the latter standard if we would know what are the real losses which the war imposes. It has recently been reported that the crown prince of Germany goes about with rags in his tires because of the lack of rubber in Germany. I do not know how the crown prince feels about this. Certainly our papers make much of the supposed loss of dignity which it imposes. But if the story be true the physical burden which the crown prince imposes on Germany is a slight one. He might estimate his injured feelings by the million but in physical

terms they would not be worth noticing. It is also said that the ladies of Germany are now compelled to wear wooden shoes because of the lack of leather. Here again we have a severe subjective loss, due to the imposed degradation, but measured in objective terms the wooden shoes place but a slight burden on the national resources. A million iron crosses have been distributed to German soldiers. The joy of this may be great but the physical cost is slight. In contrast it is said that in Paris the demand for jewelry never was greater than at present. If the Germans take their reward in iron crosses while the French demand gold and precious stones the one has a slight physical burden of the war while that of the other is heavy. The physical cost of supporting the German people is probably not over 60 per cent of what it was before the war. This leaves about 40 per cent to be devoted to military purposes. A long war of the present magnitude could be indulged in on this basis if the civil population will put up with their present sacrifices. War is a shifting of expenditure not its increase. In contrast to this the physical cost of supporting the allied nations has probably increased. Their war burden is thus an extra burden that cuts in on physical resources. The increase of the physical cost of supporting America's population is perhaps 20 per cent greater than before the war. We think ourselves worth forty billion dollars more than five years ago and rejoice that we are free from debt instead of owing billions to foreign investors. But this estimate of values is subjective. In proportion to population our physical output is not much greater than it was ten years ago.

#### WHERE WAR BURDENS SHOULD REST

It is the misfortune of discussions of taxation that investigations start with the wrong problem in mind. That men feel badly when taxes take from them their income may be taken for granted but to measure these feelings is an impossibility. Discussions of justice and morality likewise involve subjective elements which no one can measure. They are matters of feeling and it is inevitable that each one should view his burden in the light of his education and class interest. In a complex society like ours this leads to a useless wrangle about the shifting of taxation making taxation a distributive problem with all the uncertainty in which every problem of distribution is involved. Good taxes thus become those which

somebody else pays. We should not tax the laborer because that reduces his standard of living. We should not tax capital because that would limit production; we should not tax profits because that would reduce the motives for activity. And so it goes, with the result that our revenues are inadequate to meet expenditures. It only puts off the evil day to issue bonds, for in the end new taxes must be imposed to meet the increasing deficit. It is therefore a new attitude which is needed and not a further elucidation of our feelings and antipathies.

Taxes are burdens on some one's income. What principle should we employ to impose them? If objective instead of subjective tests are to be used there can be but one answer: *taxation should fall on advantage*. It is what one person has which others have not that should bear the burden when taxes are imposed. Every invention, every change in production, every increase of human energy, every economy in consumption creates a surplus which abides. This may be reserved for public benefit or be permitted to pass into private hands to be used in personal consumption. An increase of taxation means a larger use of this fund for public purposes. In times of peace but a small part of this surplus is taken for national uses. In this country not more than 10 per cent has been demanded; but under new conditions especially in large cities a greater proportion is needed by the public. The war has thus forced the nation to face a problem which time would in time have forced on public attention. Instead of 10 per cent, the nation now needs 30 per cent if revenues are to meet current expenses. Some objective measure of advantage must be found by which the burden may be so distributed that production may be interfered with to the slightest degree. Our feelings and class prejudices must be set aside and the facts faced.

#### THE MEASURE OF ADVANTAGE

The Ricardian theory of rent was the first to state the difference between earned and unearned income and thus to show that land rent was a surplus to which the recipient was not entitled for any legitimate service. This fund has rightly been held as a fit object of taxation for on it taxes may be placed which will not be burdensome to industry. So far good, but a curious intrusion of a psychic fallacy gave it a one-sided interpretation which permitted a sound

doctrine to be used for class advantage. It was assumed that the subjective cost of labor equalled the pay it received and thus all the surplus of society went to the landlord as rent. The wage fund theory was responsible for this view but its repudiation by later economists has not yet led to the broader view which newer doctrines permit. I shall make no attempt to measure the feelings of the worker of today. For aught I know he may feel worse working eight hours than his forebears did working twelve hours. He may also get less pleasure out of meat and bread than did his ancestor from the meager diet which earlier times permitted. But objectively considered he does share in the surplus modern industry has created and this fact, not his class feelings, should be considered where taxes are laid. But the error here is a slight one in comparison with the type of reasoning other classes use to justify their income.

It is assumed by the capitalist that he has a subjective pain in saving which corresponds to the rate of interest he receives. He asserts that the return on typical investments yield no surplus above the pain of abstinence and that therefore his income should be exempt from taxation. But if we use objective measures we see that the possession of capital exempts him from much misery which other classes are forced to endure. When we see the acts and the pleasure of capitalists it is hard to reconcile their plenty with the existence of a pain not revealed in their looks. Objectively the possession of capital brings pleasure and a freedom from evil. These facts and not their hidden ills should be considered by the government when it is deciding on public policies involving sacrifice. The shortcomings of the subjective standards are equally evident in the field of income. The larger income does not imply increased exertion or greater sacrifice, but a better education, better health, more energy and more fortunate conditions. Objective evidences of suffering are absent and instead there are many evidences of exemption from life's ills. Income is thus the measure of advantage and not of effort, of situation and education and not of heredity. If this income is due to education a pleasant school life replaces the early toil of those deprived of schooling. If the difference is in heredity the gains are due to what happened ages ago and not to the recipients of present income. How can a white man claim that his superior income is due to his personal exertion as compared to an

individual of the colored race? His advantage is as much unearned as is that of the landlord who lives off the proceeds of a favorably situated lot.

In the same family or in the same racial group the superiority of income due to the presence of superior traits is not the result of what the recipient has done but of his good fortune. Inheritance is not an even result going alike to all members of a family or group. The Mendel laws of unit inheritance shows that traits may be recessive in particular individuals and dominant in others. Two brothers may thus have radically different traits although their ancestry is the same. The superiority of the few over the many is a valid inference of the Mendel laws. Only a few have an abundance of those traits which make for financial success. In a rough way it may be said that of four children with like inheritance one will be superior, two mediocre and one a failure. This is about the proportion of strong and weak which we find in actual experience, thus giving a practical verification to the law in question.

To make my point I need not show in just what proportion the income of the nation will be distributed among these groups. The essential point is that the traits of the superior individual are not due to his exertion but to his advantage. This may be in education, in position, in race or due to the operation of Mendelian laws but after all it is advantage and advantage should be taxed. This does not mean that A who has an advantage has no better claim to it than B who is without this advantage. It is not the distributive problem that I am trying to settle. The real problem is what claim has the state to the income due to the advantages which the favored persons or classes have? There can be but one reply. The state represents the past and the future; the present recipient of income only the present. His superior income is due to the past of which the state and not he should be the heir. The permanent needs of the whole community are thus placed above that of particular persons and the future in which these individuals will not participate gets the advantage of the accumulations of the ages which become objective in present income.

In the use of these objective standards only two classes should be recognized; those with a deficit of income and those with a surplus. Ideally the line dividing the two classes is that income which permits the continuation of family life under normal conditions



coupled with a complete nutrition of all its members. It is not enough to preserve individuals; we must preserve the family. This means a childhood free from toil and an old age without care. Couple these facts with the cost of complete nutrition for the family at all times and we have the sum that divides a life of deficit from one of surplus. This line is not hard to determine for we have the facts that show the cost of family nurture. Eight hundred dollars represents a minimum as prices were before the war. It is certainly not less than \$1,000 at the present time. Those below this limit lack in a physical ability to contribute to the war. Those above the limit have a surplus they could spare. As against the claims of the state no class sharing in this surplus has a special claim to consideration above other classes. All families below the accepted income should be regarded as the nation's wards and treated accordingly. Were we to give them more instead of depriving them of what they have, the national surplus would be increased and the net power to carry on a war would be enlarged. By this I do not mean that these struggling families cannot be made to contribute to the support of the war. But their contribution must come through increased efficiency and not through imposed burdens. Just those things which we should have done in times of peace but neglected to do should be done on a large scale in war time. We should reduce sickness, cut down the hours of labor, have better sanitation and teach new ways of living which will promote economy and efficiency. All these measures and many more like them can be suggested which will increase the national surplus and thus enable the prosperous to bear more readily the burden of the war. But the taxation of the nation's wards is always detrimental and gives no compensations which enable others to carry on the war.

Nor do I mean that we should not encourage thrift and help people below the normal income to shift their consumption in ways that permit saving. This we would do in times of peace and should do more persistently in war time. But the means of doing this are misunderstood because of a lack of appreciation of the motives of the poorer classes. There is among them but little appreciation of distant welfare. The pressure of immediate wants is too great to inculcate a vision of the future happiness but there are strong motives to provide for such objects as they visualize. A poor family will pay high rates to insure a proper funeral for a dead

child although no motive exists to educate the living child. Much saving takes place to bridge over epochs of unemployment and some to provide against sickness. A little higher up in the scale of living the desire to own houses is an effective motive causing building and loan associations to thrive. In country districts the ownership of farms makes an appeal which is effective so long as land is of low enough a price to permit a purchase. But all these motives fail when future weal stands alone. In a 4 per cent railroad loan a farmer will not invest and the lack of motive is still greater among the industrial workers whose saving motives are more difficult to arouse. But this does not mean that these people may not be appealed to by a war loan. The rate of interest, however, must be much higher than that now offered. The lesson of the war will show that the "big stick" disguised in forms of patriotism will not increase saving above its present amount. High rates of interest would do this with the effect not only of helping to carry the war to a successful close but of transforming a large part of the nation's wards into normal citizens. But this change should be voluntary appealing to motives which the nation's wards understand. It is their psychology and not that of the upper classes that we should study. If this is done the primary burden of the war must fall on those with a surplus income who now have their wants supplied above the minimum of well-being.

It is this objective surplus and not profit commercially considered that must be found and measured. The subjective elements in older estimates made the costs of production seem larger than they are. If I pay thirty dollars for a suit of clothes I pay for certain material which must be replaced and for certain quantities of food and shelter which workers require. But much of my thirty dollars goes to compensate the feelings which producers have. This sum need not be paid or its payment may be delayed. The owner of horses estimates their cost by the food he gives them and by the cost of the care involved in their keep. He does not regard the feelings of the horse nor put their equivalent in his estimates of cost. If from day to day they show no deterioration in objective appearance he regards the sum given for their support as his expense. The same is true of a population. The physical cost of a people is the amount needed for bodily welfare. The difference between this cost and the output of industry is the surplus.

Whoever shares in this has something which he might give up without reducing industry and this amount fixes the limit of taxation. When we realize this we can see why Germany stands the burden of the war so well. The people grumble and occasionally revolt, but there is no reason why this burden should not be borne for years if the will of the German people is equal to the sacrifice demanded. What they have done we can do on a larger scale because our surplus measured objectively is much larger than theirs. When it is asked can the proposed war expenditures be borne by the American people there is but one answer to be made. They can be borne and even more than the proposed ten billions can be set aside without cutting in on the sum needed to repay physical costs. But if it is done there must be no waste nor any compensation for outraged feelings. If we do what we can and avoid what we should we can bring the war to a successful close.

Many contend that in some way a part of the burden of the war may be shifted to future generations. To them the advantage, why not to them the cost? The difficulty in this solution is that the cost of war is in present goods. It is what we have which must be given for war ends and not what our descendants may acquire. War is a consumer whose needs cannot be postponed. The soldiers are preferred consumers, who must be cared for better than before. It is only the residual left after the war needs are supplied which the public can have. War thus forces a transfer of the social surplus from those who now enjoy it to those engaged in military operations. Each year of the war must therefore square its own accounts unless at the beginning of the war there is a stock on hand which may be used for the initial expenditure. Before America entered the war the accumulated stock of the world had been used up. Our problem is thus a simple one. We must save from ordinary consumption enough to supply the needs of our army. This reduced consumption may be forced, or voluntary, and the two methods of financing the war hinge on the difference. Forced saving operates through an increase of prices. The consumer has to pay more for goods with the same or a reduced income. He must therefore contract his consumption. The high prices make profits and the government borrows the net gains of the profiteer to carry on the war. Forced saving by this process turns over a part of the people's daily consumption to the recipients of high prices. What the people save is

thus given to a privileged class and they loan it to the government.

This is the essence of carrying on the war by means of loans. The people pay for the war by their reduced consumption, the benefit of which goes to the profiteer. In the end the people pay for the war a second time when they redeem the loan through future taxation. The people thus make additional burdens for themselves at some future time. *War loans are war profits.* They are the gains which favored individuals make from the war and do not in the slightest way reduce the burden borne by the people. This is not a new doctrine but one often explained by economists. But sound economic is lost sight of in the stress of a financial situation and old fallacies blossom forth with the freshness and vigor of new creations. If the high prices were occasioned by an increase of paper money, the advocates of it would have to blush for their logic, but when the same inflation is produced by a bond issue a quibble is possible which permits a flood of new argumentation over a point long ago settled. In any real sense inflation is an elevation of goods above their physical valuation. One can readily see that an increase of paper money deceives people as to their real possessions and entices them to expend above their means, and thus causes an overconsumption which brings on a crisis. Bond issues have the same result in another way. At a time when wealth is decreasing it seems to be increasing and thus induces people to expend lavishly when their consumption should be curtailed. We are said to have had two hundred billions of wealth at the beginning of the war. The government spends twenty billions leaving one hundred and eighty billions. The public instead of seeing this and acting accordingly add the twenty billions of bonds to their wealth as though it were an addition instead of a loss and call themselves worth two hundred and twenty billions. This is a deception like that of paper money inflation and equals it in its bad effects. Did this doctrine deceive only the common people it might be put up with, but editors, bankers and government officials are equally carried along with the current of popular thought. Our national income before the war was estimated at thirty billions. A member of the Federal Reserve Board recently said it was now fifty billions. Just how the destruction of the war could increase the income of the nation by a half he did not explain. It is plain he was adding in our losses as though they were

a gain and thus deceiving himself as to what our real income is. This attitude is so general that it cannot but encourage the opinion that the war can be carried on with a profit and hence permit of an increase of consumption at the very time when a sharp contraction is the only means of saving the nation's credit. Our great task is to make people realize the need of economy and this can be done only by saner estimates of the effect of the war on property and income. The entire amount by which value exceeds property is an inflation which can be cured only by the reduction of property values to their normal level. Government bonds are not the only form of inflation nor did the rise of prices begin with the war. It was going on in the dozen years of advancing prices before the war. The two hundred billions of wealth we were supposed to have at the beginning of the war really contained fifty billions of inflated values. It would have been a different task to have found one hundred and fifty billions of actual property at that time. If now we use twenty billions in war expenditure and add this amount to our reputed wealth every dollar of our actual wealth will be estimated at double its amount and be the basis of a double expenditure.

Our annual expenditure may be fifty billions but if so there is a big gap between receipts and expenditures which will soon bring the nation into financial straits. Bond issues are not a way out but a species of deception for which the public must pay a heavy price. They suffer and pay for the war; they will suffer and pay again when the bonds are redeemed. And there will come the greatest suffering of all in the financial crisis which brings inflated values back to a normal basis. Three payments and perhaps five are what this financial method imposes. Our liberties are worth the price, but before payment is it not worth while to ask how can a war be carried on with but one payment and with no inflation of values?

A good system of taxation involves more than a decision as to taxes and the machinery for their collection. The theory of values and equivalents is involved and with them must be correlated all the other mechanisms by which prices are influenced. Important among these are the restraints on consumption. We may let prices go up, and then tax people for the additional amounts needed or we may restrain consumption so that the amount saved flows into the government's coffer without an increase of price. If a third of the annual expenditure for goods must be turned over to the state, re-

strictions will effect this more readily than taxation and must be the major means by which the transfer is wrought. A prohibition of liquor traffic would reduce the demand for goods and thus prevent the rise of prices to the level they otherwise would reach. Another inroad might be made by checks to conspicuous consumption. A third of what the nation consumes has little bearing on physical welfare and on this part effective restraints should be placed.

A policy of education is needed as well as of restriction. Evolution exerts a steady pressure in changing consumption from more to less costly means of gratifying human wants. If the restriction operates to favor evolution the change is permanent. The broken habit of custom will not be restored when the restraint is removed. But if the change is a mere blocking of urgent desires then the removal of the restraint means a sinking back into an earlier state with a vast amount of increased dissipation. This relapse is too often seen after the restraints of war are removed. An epoch of dissipation has a train of evils worse than war itself. These facts make restraints and education of such importance that no scientific scheme of taxation can be made workable without their aid. On the one hand they cut down the eagerness to spend and on the other they force adjustments which abide. It is to them and not to bond issues to which the nation should turn and when they are in operation the real burden of the war can be met by taxation. Taxation is not a sham pretending to give when it really takes. It is a present burden which cannot be shifted to future generations.

Distributive problems are out of place in a scheme of taxation because they confuse the public as to the point at issue. Property owners like to talk of shifting the burden on someone else and popular agitators are likewise fond of showing how this is done. If either are right my position is unsound. If both are wrong then a view of taxation is possible which will show where the burden really lies. The whites of the south may get satisfaction out of the burdens they place on the negroes and among the latter suffering may result. But if we disregard these subjective feelings the net result is that the whites put a heavy financial burden on themselves by this repression. An increased efficiency of negroes would mean an increased income for themselves. There is no way they can shift this financial loss on other shoulders. So too employers may get satisfaction by discharging workers at will but they cannot avoid the large labor

turnover that results. Every downward pressure on workers decreases their efficiency and reduces the net surplus of industry. It is impossible, therefore, to put a burden on workers that will not take from employers more than the laborers lose.

If the prosperous must bear the ultimate burden and any attempt to shift is only at their cost it is not difficult to decide where new taxes should be imposed. They should fall on the net surplus of society, and should be proportioned to the surplus of each class or individual. The income tax seems best fitted to meet these requirements but in reality it has a defect which makes its operation one-sided. Income is a measure of immediate advantage but not of ultimate advantage. Suppose the income of a given industry is increased by \$50,000. This is income and rightly to be taxed. But the presence of this income will increase the value of property by a million dollars if interest is 5 per cent. This million dollars the income tax does not reach but is as fit an object of taxation as is the original income. The ultimate advantage of an increased national return thus shows itself not an income but in increased capitalization. It is this untaxed capitalization which new taxes should reach.

If the prosperous object to this solution can they shift the burden on any one else? If twenty billion dollars in bonds are issued instead of the needed liquidation of values they start an inflation which produces a still greater deficit. Every financial scheme to shift the burden breaks on this rock. It produces suffering among other classes but gives no relief to the net burden of the prosperous. Every deceptive device comes back to claim compound interest. They can pay for the war once if they pay the bills as they come due. They can pay for it as many times as they please by trying to make future generations pay. An individual may escape his burden by schemes that put the burden on others. He may take his chance in a panic and gain where others lose. But these devices do not take the burden from the prosperous. The individual who avoids his just burden punishes his friends and not the laborers or the community. They will suffer but their suffering brings no relief to the prosperous. All improvements increase net income; all burdens fall on it. Were this simple proposition once understood we might face greater burdens than this war will impose and still remain financially sound. The burden of today will come back to the pres-

ent holders of income in the surplus of tomorrow. If inflation is an evil then it must be met by cutting down the national valuation of assets until they correspond to our physical possessions. We must not deceive ourselves into thinking we have two hundred and fifty billions of wealth when we have only one hundred and fifty billions, nor can we think that war is a process of increasing wealth when it merely inflates values. A liquidation tax is the only means of meeting this situation. If a man is worth two hundred and fifty thousand dollars and had one hundred thousand in debts he would not be made poorer by paying his debts and having one hundred and fifty thousand of clear wealth. The situation of the nation is this on a large scale. We spend money but instead of recognizing it we cover it up by calling our liabilities assets. To tax the nation ten billions does not differ in its ultimate effects on wealth from a bond issue to a like amount. In either case we are ten billions poorer. In one case we see it and adjust our expenses accordingly, in the other we rush on into new extravagances. A risk is run for which there is no compensation.

It is therefore the present inflated values which should be reached by any sound system of finance. A liquidation should be forced which will bring inflated values down to a level with physical valuation. People are not made poorer by this process. They are put in a position safely to take advantage of new industrial opportunities. We should therefore take a stock of national wealth and make an assessment against it. He who gets the surplus when the nation prospers should pay back when the nation is forced to enlarge its expenses. The income tax is one means of reaching this surplus but a far larger part of it goes to increased values and hence stands on the books of each individual as property. The increase of values is thus a legitimate source of taxation and it is this increase which should meet the special burdens of a war. We cannot get at the annual increase of values as readily as of incomes because incomes are regularly reproduced while it is often years before an increase of property values shows itself. A ten-year period would meet the situation fairly well and if a decennial revaluation of national wealth were made the increase thus revealed should be used to meet emergencies. If such a scheme were adopted the first assessment should be on all property for we have no ready means of distinguishing its parts. But the scheme once in operation would permit



subsequent taxation to be based on the increase of values. In practice it would work out something like this. I assume that it would be combined with an inheritance tax and that the rate of taxation is 5 per cent.

<i>1918</i>	<i>Amount of Property</i>	<i>Tax 5 per cent</i>
Howard Smith	\$240,000	\$12,000
<i>1928</i>	300,000	
	—240,000	
	<hr/> \$60,000	3,000
<i>1932</i>		
Estate of Howard Smith	\$320,000	16,000
Howard Smith Jr. (Inheritance)	120,000	6,000
<i>1938</i>		
Howard Smith Jr.	160,000	
	—120,000	
	<hr/> \$40,000	2,000

It is plain that the net wealth of this family is not reduced by the liquidation. They are merely put in a sound financial position and thus avoid the penalties which wild financing imposes. Nor does it prevent the regular increase of values which is the legitimate result of national property. They are only prevented from over-estimating the real increase and thus checked in the tendency to over-indulgence. A good financial scheme combines restriction on consumption, and a process for the liquidation of debts. Scarcely any use is made of restriction; the rate of interest offered is too low to encourage saving and the process of liquidation has not even been discussed. It is necessary to use treasury notes freely for the proceeds of taxation come in too slowly to meet current expenses. But short-time notes should not be issued until expedients are adopted to redeem them. We may properly ask the banks to carry temporary burdens but government bonds make for them bad permanent investments.

If these legitimate sources of revenue are avoided the only remaining expedient is a bond issue. The burden of the public is thus

an indirect one. They pay for the war through high prices which make profits for other people to invest in bonds. War bonds and war profits are thus the same fund and force a double payment in the end by the people. Such financing is easy for the first year, makes difficulties the second year and creates impossible conditions in the third. If we are to go ahead according to present plans it is to be hoped that German resources are nearing exhaustion. It will save us from many threatening evils.